

CONTRACT MANAGEMENT FRAMEWORK

“The City of Heritage”



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1 Introduction to the CMF

1.1 Application

The CMF shall be applicable to all State Institutions. All Institutions must develop or update their policies, procedures, systems and competencies to align with the principles captured in this CMF.

The CMF consist of 3 documents-;

- This Contract Management Framework;
- Contract Management Guide. This document is to assist in the implementation of the Framework; and
- Guideline for implementation of a Contract Management System. This document is to assist in the creation and management of a contract management system.

1.2 Purpose and scope of the CMF

The Contract Management Framework (CMF) is a high level document that sets out the requirements for government institutions pertaining to the management of, and accounting for, contract agreements.

This document serves as a framework only, and practical guidance on application of the framework is contained in a separate Contract Management Guide (CMG).

The CMF requires an organisation wide approach to contract management including:

- identification of all contracts and stakeholders;
- classification of contracts for management purposes; and
- management of all stages in the contract life cycle.

Since all transactions are the result of a contract (whether explicit or implied), the introduction of the CMF will facilitate improvements in financial management and lead to:

- reduction in costs;
- increases in revenue; and
- enhanced service delivery.

The CMF and CMG do not delve deeply into the technical application of accounting standards or the specifics of contract law. The focus is on setting out the requirements for adoption of appropriate management policies, procedures, techniques and disclosures.

There are substantial regulations and guidelines on the “Procurement” phase of the supply chain including requirements for bidding for and awarding of contracts. These can be viewed at www.treasury.gov.za/divisions/sf/sc. The CMF and CMG cover management practices relating to contracts in general and do not provide detailed discussion of the procurement phase of contract management.

In summary, for the purposes of the CMF and CMG, contract management encompasses:

- management of all contract agreements during the entire contract life cycle; and
- correctly accounting for all contracts.

1.3 Importance of contract management

Every transaction undertaken by an organisation involves a contract whether explicitly agreed in writing, or implicitly implied through actions. Properly managed contracts can ensure that services are delivered within specification and at the agreed cost. Improperly managed contracts may impact negatively on the institution and government as a whole. Adverse effects of poor contract management include but are not limited to:

- poor supplier, buyer or other stakeholder relations;
- negative public perception;
- protracted legal disputes;
- cost overruns;
- goods and services outside of specification; and potentially
- complete service delivery failure.

Hence, good contract management is essential for good financial management and will contribute greatly to the effectiveness and efficiency of service delivery.

1.4 Managing contracts

Contract management records, procedures and systems (whether manual or computerised) may vary significantly from one institution to the next depending on size and nature. Each institution is required to develop policies, procedures, systems and competencies within the scope of the generic framework following the guidance issued in the CMG.

For the purposes of the CMF, contract management activities refer to:

- identification and classification of contracts for management purposes;
- recognition, measurement and disclosure;
- planning and budgeting for contracts;
- oversight of contract management;
- resourcing contract management activities;
- document and information management;
- relationship management;
- performance management;
- payment, collection, incentives, and penalties; and
- risk management.

Each contract across the entire institution must be managed throughout the contract life cycle based on the level of management control appropriate for the classification of that contract.

For the purposes of the CMF, the Contract Life Cycle spans from planning for the contract through to contract closeout:

- planning;
- creation;
- collaboration;
- execution;
- administration; and
- closeout / renewal.

1.5 Correctly accounting for contracts

Accounting for contracts is concerned with recognition, measurement and disclosure of the financial implications resulting from contracts. As mentioned above, all transactions are contractual, whether explicit or implied.

Public Entities currently apply the relevant accounting standards and all other government institutions are gradually phasing in Generally Recognised Accounting Practice (GRAP). During the phase in period, government institutions not currently applying GRAP are required to apply the Financial Reporting Framework Preparation Guide (Preparation Guide) issued annually by the Office of the Accountant General (OAG) in the National Treasury.

GRAP and the Preparation Guide set out detailed requirements for recognition, measurement and disclosure of all classes of transactions.

2 Contract management in the public sector

2.1 Why manage contracts in the public sector?

Apart from legal requirements to properly manage contracts, a private sector entity will look to ensure the most efficient investment of resources in the pursuit of profit maximisation and therefore return on investment.

A public sector entity is also looking to maximise return on investment in order to deliver more services or a higher level of service to the community and other stakeholders served. Where services are paid for by rates, taxes, tariffs or service charges, the question of accountability for public funds arises.

Financial management and related governance reforms being introduced in the public sector in South Africa are seeking to improve service delivery to all South Africans through securing sound and sustainable management of the financial affairs of government. Improved financial management will lead to:

- improved information for making policy choices (allocation of resources to programmes);
- more efficient use of resources in delivering the chosen programmes; and
- increasing the rate of delivery of basic services and associated elimination of service delivery backlogs.

This is achieved primarily through:

- enhancing transparency and credibility of information contained in budgets, in-year reports and end of year reports such as the annual financial statements and annual reports; and
- improving financial management and internal controls.

Transparency and credibility supports the concept of accountability. Information with these attributes can be more reliably used to hold government accountable for delivering on promised service delivery within approved budgets. This corresponds with an increased focus on measuring outputs and outcomes and not just what was spent and what was received.

Implementation of commitment and accrual accounting by all national and provincial departments will lead to increased transparency and credibility of budgets, in-year reports, annual financial statements and annual reports. For example, lease contracts which are substantially the same

as borrowing for assets will require disclosure on the statement of financial position (balance sheet) for the assets being leased and for the liability inherent in the finance lease.

Improved contract management in the public sector in terms of management practices and financial disclosure can, for example, lead to:

- increased awareness of all forms of contracts and their implications;
- identifying non-performing suppliers, buyers and other stakeholders who are either performance managed or replaced;
- development of strategic supplier, buyer and other stakeholder relationships with a view to improving service delivery and reducing costs; and
- better value for money achieved in the acquisition and sales of goods and services.

Savings generated through improved contract management may be reallocated to reduce cost of services or provide additional services; and may contribute to the elimination of service delivery backlogs.

2.2 Legislative and regulatory framework

The legislative framework provided by the Public Finance Management Act (PFMA), regulations and guidelines focuses on improving financial management and service delivery.

The preamble of the PFMA provides the scope and focus in terms of improving financial management in the public sector.

Section 38 of the PFMA places responsibility on the accounting officer for financial management functions. Section 44 provides for the assignment of powers and duties by the accounting officer to other officials and section 45 details the responsibilities of those other officials. Sections 51, 56 and 57 repeat these responsibilities with regard to public entities.

In particular, the above sections of the PFMA make reference to ensuring:

- effective, efficient, economic and transparent use of resources; and
- all contractual obligations are settled and monies owing are paid within terms.

The Treasury Regulations, 2005, issued in terms of the PFMA have limited provisions relating to contract management including the following:

- 8.2.3 requires creditors to be settled within 30 days from receipt of invoice or settlement date or court judgement in the case of civil claims;
- 15.10.1.2 states that sound cash management includes avoiding prepayments for goods and services unless required by the contractual agreements with the supplier;
- 16.7.1 states that the accounting officer or accounting authority of the institution that is party to a Public Private Partnership (PPP) agreement is responsible for ensuring the PPP agreement is properly implemented, managed, enforced, monitored and reported on, and must maintain mechanisms and procedures for:
 - measuring the outputs of the PPP agreement;
 - monitoring the implementation of the PPP agreement and performances under the PPP agreement;
 - liaising with the private party;
 - resolving disputes and differences with the private party;
 - generally overseeing the day-to-day management of the PPP agreement; and
 - reporting on the PPP agreement in the institution's annual report.
- 17.2 sets out retention periods for documents including contracts, and all other documents relating to purchase of goods and services.

The Contract Management Framework, set out in this document, builds on the above and provides additional guidance on contract management requirements for government institutions.

3 Contract management framework (CMF)

3.1 Overview of the CMF

The CMF is applicable to all national and provincial departments and public entities. It is a generic framework which enables departments and entities to approve their own policies and procedures relating to contract management. The framework, depicted in Diagram 3a below, provides direction on how government institutions must:

- ensure appropriate policies and procedures are in place;
- employ appropriate contract management practices; and
- recognise contractual obligations in the annual financial statements.

Diagram 3a: Contract management framework (CMF)



Note that any reference to “systems” refers to manual and or computerised systems. Departments must not delay implementation of the CMF due to computer system constraints. If such constraints exist, manual systems must be implemented to ensure compliance.

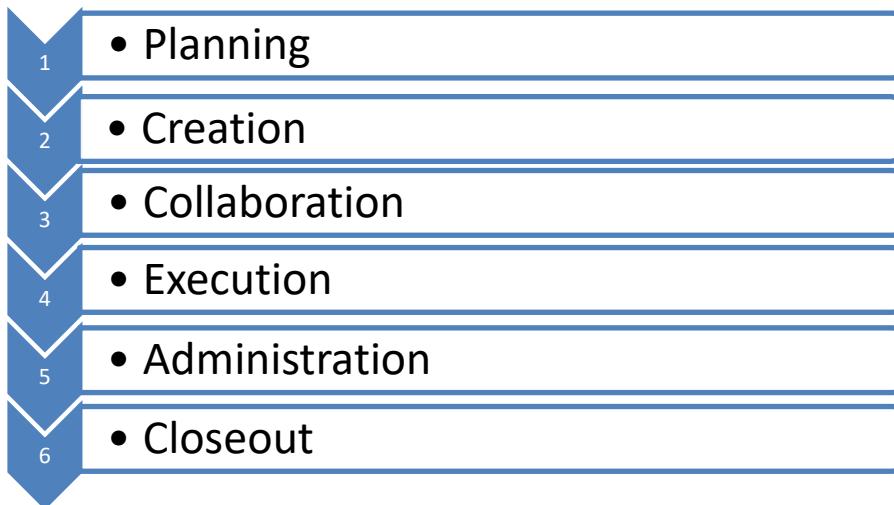
The CMF should be considered in the context of the Contract Life Cycle as described in section 3.2 below.

3.2 Enterprise contract management and contract life cycle

The CMF applies an Enterprise Contract Management (ECM) approach requiring identification, classification and appropriate management of all contracts throughout the institution.

Further, contract management must be applied throughout the Contract Life Cycle as depicted in diagram 3b below.

Diagram 3b: Contract Life Cycle



Planning

This stage refers to consideration of contracts during planning and budgeting processes. These processes will identify the need for contract creation and when this must happen to ensure delivery can occur as approved in the budget.

Creation

During creation, the contract author will decide on the most appropriate wording to give effect to the intended outputs and outcomes and prepare the first draft of contract documentation.

Collaboration

Collaboration is the drafting and negotiating process including internal and external reviews to ensure that the contract will give legal effect to the requirements of all parties to the contract.

Execution

Execution is the act of signing the contract, making it legally enforceable and formalising the terms and conditions agreed to.

Administration

Administration includes monitoring delivery under the contract to ensure that it achieves its original objectives and effecting any necessary changes to the contract.

Closeout / renewal

The closeout / renewal stage includes necessary actions to end or renew the agreement and associated performance review.

3.3 Identification and classification of contracts

Government institutions must compile a Contracts Inventory which lists and classifies all contracts. Each manager at the level of Chief Director and above (or similar for public entities) must maintain a Contracts Inventory for the contracts they are responsible for.

A classification system must be established which identifies levels of management control for classifications of contracts taking into account at least the:

- contract type or nature;
- strategic importance of the goods and services being purchased or sold;
- contract value;
- contract duration; and
- contract complexity.

Policies and procedures must then be established and implemented to deal with the management control requirements for each category.

Each institution must reconsider their Contracts Inventory, classifications, policies, and procedures at least annually.

3.4 Recognition, measurement and disclosure of contracts

Recognition, measurement and disclosure of the financial implications resulting from contracts refer to treatment of transactions in the annual financial statements, disclosure notes and annexures. Good management practices will facilitate proper and full disclosure which in turn will lead to improved decision usefulness of financial information.

Public entities already apply relevant accounting standards.

The phase-in provisions for the CMF require national and provincial departments to be applying GRAP for the 2012/13 budget. Departments must continue to implement procedures and systems to facilitate compliance.

In 2010/11 and 2011/12 modified cash accounting may be applied in accordance with the Preparation Guide although earlier compliance with GRAP is encouraged. The OAG will provide guidance on disclosures each year in the Preparation Guide.

3.5 Planning, budgeting and reporting cycle

A comprehensive review of all existing and proposed contracts must be undertaken during:

- planning and budgeting processes; and
- preparation of audited annual financial statements (AFS) and annual report.

Institutions may combine the above review processes.

In-year reporting processes must also include a contract review component. However, for in-year reporting purposes, contract reviews may be based on exception and limited regular reporting as necessary to appropriately manage existing contracts and plan for proposed contracts.

3.6 Oversight of contract management

The accounting officer or accounting authority of the institution is responsible for ensuring contracts are properly implemented, managed, enforced, monitored and reported on, and must take all reasonable steps to ensure that:

- contracts are properly enforced;
- contracts are classified according to the level of management intervention required;
- contracts are monitored and managed appropriately according to their classification;
- a single person or committee is allocated responsibility for driving institution wide contract management performance;
- roles for contract owners, contract managers and other stakeholders are clearly defined;
- appropriate delegations are in place to allow role players to carry out their responsibilities;
- clear procedures for handover from contract award to contract management are in place;
- contract management plans are implemented where appropriate, and focussed on outputs and performance;
- contract management processes and procedures are aligned with organisation wide governance and risk management processes, and performance is reported through established governance channels;
- ongoing contract management training is provided during induction as well as regular refresher training;
- there is an annual review and adjustment of contract management policies, procedures and guidance with a view to continuous improvement in contract management;
- there is regular assessment and evaluation of the effectiveness and efficiency of contract management activities including an assessment of the costs of the contract management function; and
- policies and procedures are in place in terms of:

- identification and classification of contracts for management purposes;
- recognition, measurement and disclosure;
- planning and budgeting for contracts;
- oversight of contract management;
- resourcing contract management activities;
- document and information management;
- relationship management;
- performance management;
- payment, collection, incentives, and penalties; and
- risk management.

3.7 Resourcing contract management activities

Contracts must be appropriately resourced in line with their classification for management purposes including:

- appropriate systems (manual or computerised) in place for management control and monitoring;
- contract owners and managers and other advisors have appropriate skills and qualifications to carry out the contract management activities;
- skills and qualifications are accurately detailed in job descriptions;
- salaries are commensurate with duties;
- appropriate training and support is provided to contract owners to assist in their dealings with the contract management team and other stakeholders;
- contract managers are involved during the tendering / contract award process and or there is a handover from staff involved with the tendering and award; and
- staff managing the bid and award process understand contract management requirements and the implications that awarding the contract will have on managing the contract during its life.

3.8 Document and information management

The contract documentation and associated terms and conditions, including where appropriate milestones and deliverables, must be managed according to the requirements for the category of contract including:

- record management systems (physical and or electronic) in place to ensure secure storage of, and easy access to contract documentation;
- written procedures set out strict processes for: records management; key information to be recorded for categories of contract; reporting; changes to contracts; contract closure;

- contract management system (computerised or manual) used to record and report on key information and trigger points;
- regular and ad-hoc reporting highlights satisfactory contract progress, issues by exception, and the need for contract updating due to changed circumstances;
- reporting feeds information useful for demand management back into the planning and budgeting process (assessment of quality, quantity, timing, price, and supplier);
- reporting feeds information into the inventory, asset, and liability management systems;
- information is shared as much as possible with purchasing, sales, accounts payable and accounts receivable system; and
- all role players have a clear understanding of the procedures for: extensions; varying of conditions; price escalation; any other potential contract changes; and contract closure.

3.9 Relationship management

Relationship management is a necessary extension of contract management and includes relationships with:

- external suppliers and buyers;
- internal service providers and receivers; and
- all other relevant stakeholders.

Relationship management must take into account at least the following:

- stakeholder relationships classified according to a framework appropriate for the institution to determine the level of interaction between the institution and stakeholders;
- consideration given to continuity of supplier and buyer staff for appropriate categories of contracts;
- regular contract management reviews consider existing and potential strategic relationships with a view to deliver benefits for all relevant parties;
- roles and responsibilities of the contract manager, contract owner and supplier or buyer are clearly defined and differentiated in the contract documentation and well understood by all parties;
- policies, procedures, contract clauses and practices promote and demonstrate actual formal and informal communication channels where appropriate; and
- policies, procedures, contract clauses and practices promote and demonstrate clear problem and conflict resolution mechanisms including well defined and known escalation routes.

3.10 Performance management

The performance of suppliers, buyers, other stakeholders, and individual contracts must be managed appropriately for the classification of contract including:

- policies and procedures to assess the performance of the supplier, buyer or other stakeholders in meeting the requirements of the contract are clear, well documented and communicated to all parties before signing of the contract, and prior to commencement of delivery under the contract;
- baselines, measurement metrics, methods, data sources, and collection responsibilities are agreed with the supplier before contract signing and commencement of delivery;
- performance measurement metrics are linked to service delivery agreements which are consistent with the strategic objectives of the institution;
- regular performance reviews are conducted in accordance with the requirements for the classification of the contract and or stakeholder;
- ad-hoc performance reviews are conducted where non-performance is identified outside of the regular review process;
- non-performance is addressed with at least a formal letter advising specific non-performing areas and stating remedial action/s required within specific time frames;
- good performance is recognised and communicated through established channels;
- all parties participate in joint performance reviews where appropriate, and seek continuous improvement opportunities;
- reporting is streamlined, focusing as much as possible on self measurement, with independent checking mechanisms and exception reporting; and
- the general market (outside of current suppliers or buyers) is monitored for market trends and compared to performance of current suppliers and buyers.

3.11 Payment, collection, incentives and penalties

Payments, collections, incentives and penalties must be appropriately managed such that:

- payment and collection procedures, conditions and time frames are clearly documented and communicated to suppliers and buyers (milestones, documentation required, documentation submission channels, incentives, penalties, etc);
- payments are always (100% of the time) made in accordance with the contract and commercial terms;
- receipt of monies due is actively monitored and where monies are not received within terms, immediate action is initiated to recover outstanding amounts; and
- incentive and penalty mechanisms are clearly linked to desired outcomes and specifically to the strategic objectives of the organisation.

3.12 Risk management

Contract risk must be appropriately managed such that:

- all contracts set out risk identification, monitoring and escalation procedures and mechanisms which are in line with the institutions enterprise risk management plan;
- all contracts identify contingency plans for supplier or buyer failure;
- for key suppliers and buyers, the contract manager monitors the financial health, tax compliance and overall performance of the supplier or buyer; and
- contract terms and potential ramifications around key issues including: termination; warranty; indemnity; security; confidentiality; and dispute resolution are understood by the contract manager.

3.13 Policies and procedures

3.13.1 *Contract management policies*

Contract management policies must be reviewed annually and adjusted as necessary with a view to continuous improvement in enterprise contract management.

Policies for at least the following should be developed, approved and considered each time the contract management policies are reviewed:

- Identification and classification of all contracts
- Management intervention of contracts based on classification
- Recognition, measurement and disclosure for financial reporting
- Planning and budgeting for contracts
- Oversight of contract management
- Resourcing contract management activities
- Document and information management
- Relationship management
- Performance management
- Payment, collection, incentives, and penalties
- Risk management
- Procedure manuals covering the Contract Life Cycle for all contracts

3.13.2 Contract management procedures

Procedure manuals must be maintained up to date for at least the following:

- contract classification methodology;
- reviewing existing and proposed contracts during the strategic planning and budgeting process;
- annual training plans and competency assessments;
- records and document management;
- recording of key contract information;
- stakeholder education and accreditation within relationship management frameworks;
- performance reporting structure, content, frequency and recipients;
- payment and collection;
- incentive and penalty schemes;
- risk analysis, identification, assessment and response; and
- management controls for each classification, type or individual contract covering the entire Contract Life Cycle.
 - Planning
 - Creation
 - Collaboration
 - Execution
 - Administration
 - Closeout / renewal

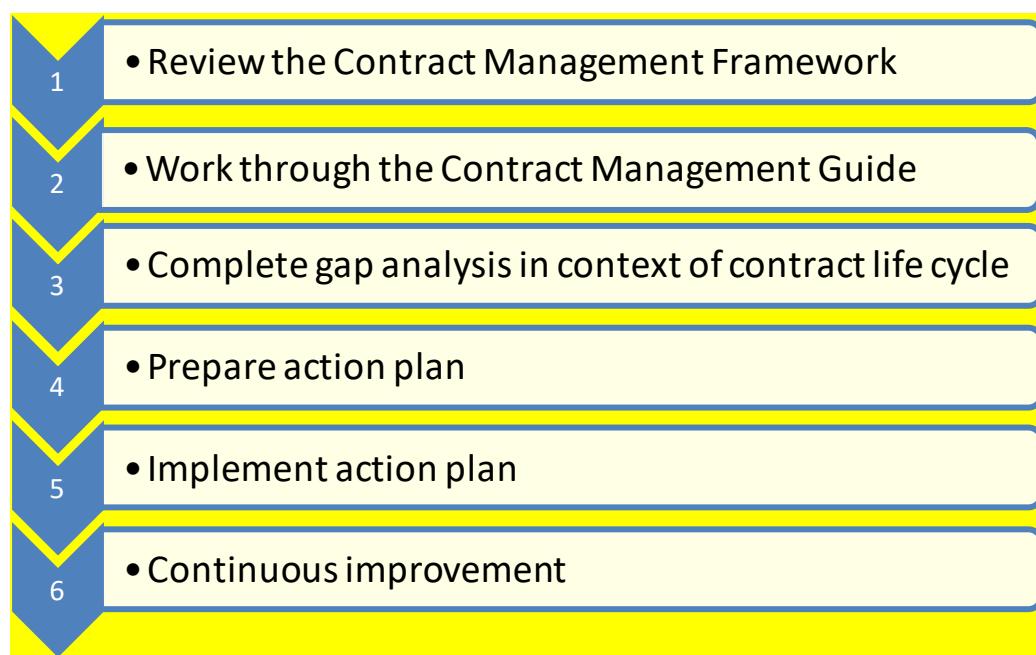
4 Implementation strategy

4.1 Contract management practices

National and provincial departments and public entities must approve and implement policies and procedures for contract management activities within the generic requirements of the CMF.

Institutions may follow the proposed implementation strategy illustrated in Diagram 4a below.

Diagram 4a: CMF Implementation Strategy



Institutions should first review the CMF and work through the CMG before completing the self assessment. The self assessment should be completed in the context of the Contract Life Cycle to identify gaps and prepare an implementation action plan. The implementation strategy recognises that institutions will need to plan for continuous improvement in contract management practices. Further detail on the proposed implementation strategy is contained in the CMG. The action plan should specify tasks, responsibilities and deadlines with a view to complying with the phase-in provisions below.

In 2010/11 national and provincial departments and public entities must review all contract management policies and practices and compare actual practice with the requirements of the CMF and CMG. Draft policies and procedures must be documented as far as possible with a view to approving all of the required policies and procedures by the end of 2011/12.

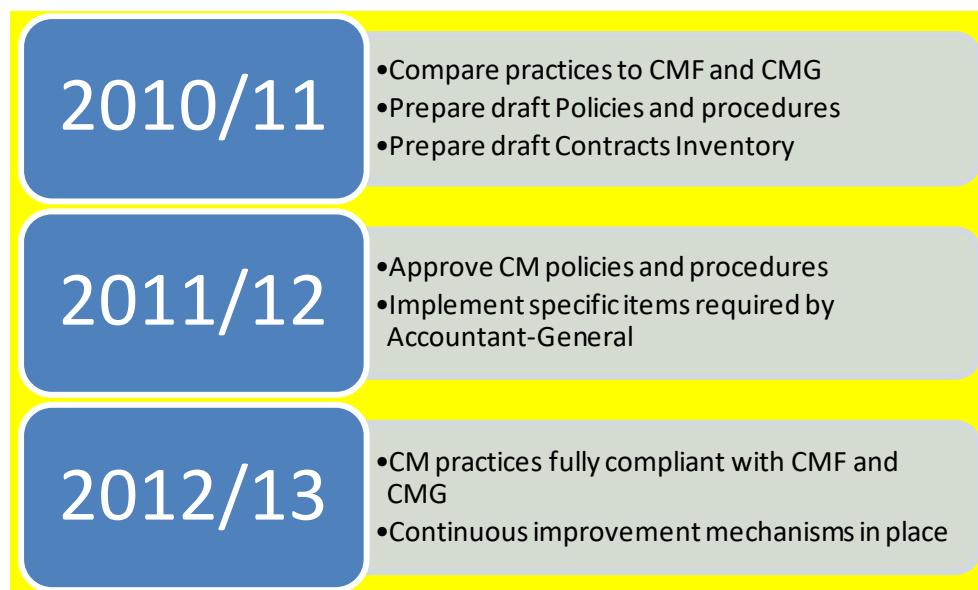
By the end of 2011/12 national and provincial departments and public entities must approve all of the required policies and procedures. The OAG will specify certain items for implementation.

From the beginning of 2012/13 contract management policies and practices must be fully compliant with the requirements of the CMF and CMG. All required procedure manuals must be in place and operational.

Existing contracts may contain legal impediments for compliance with policies and procedures approved in accordance with the CMF. If this occurs, the relevant contract conditions must be reviewed and amended as soon as practical. All new contracts and associated contract management practices must be compliant with the approved policies and procedures [and be managed according the contract life cycle](#).

The OAG will provide specific guidance each year on specific requirements for contract management practices throughout government. The road map to implement contract management practices is as per diagram 4b below:

Diagram 4b: Phase-in for contract management practices



Computerised systems for contract management

Any reference to systems or processes refers to manual and or computerised systems or processes. Government institutions must not delay implementation of the CMF due to computer system constraints. If such constraints exist, manual systems must be implemented to ensure compliance.

Government institutions are encouraged to focus on simple solutions for implementation and compliance rather than complicated solutions that carry more risk of failure. A useful approach is to review and document business process requirements, implement simple solutions immediately and plan for continuous improvement over time.

Manual systems are regarded as an interim step and efforts to automate contract management activities should be initiated as soon possible.

4.2 Accrual accounting

Public entities already apply the relevant accounting standards.

National and provincial departments must continue preparations for full compliance with GRAP standards for the 2012/13 financial year subject to financial management system readiness.

For this to be achieved, departments must ensure that contract management practices are implemented as necessary.

The OAG will continue to provide guidance on disclosures and annexures each year in the Preparation Guide to the Annual Financial statements.

The road map for national and provincial departments to phase-in GRAP standards is shown in diagram 4c below.

Diagram 4c: Phase-in for accrual accounting

